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February 12, 2004

VIA ELECTRONIC FILING

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: CC Docket No. 01-92, WC Docket Nos. 02-361, 03-211, 03-266

Dear Ms. Dortch:

Level 3 Communications LLC ("Level 3"), through its attorneys, submits this letter to set forth its opposition to retroactive application of access charges to any voice-embedded IP communications.[1] Although Level 3 does not believe that access charges should be applied to such traffic at all, the purpose of this letter is to urge that to the extent this Commission ultimately finds that access charges *are* applicable to some voice-embedded IP traffic, there is no basis in law or policy for applying that new rule retroactively. Moreover, as further discussed below, that is particularly true with respect to IP-to-PSTN and PSTN-to-IP voice communications.

As the Commission is aware, currently pending before it are myriad matters relating to the proper regulatory status of voice-embedded IP traffic. A central issue in that debate is whether and to what extent the economic and regulatory constraints of the circuit-switched access charge system should be superimposed on innovative new voice-embedded IP applications. AT&T has, for example, argued that the Commission should issue a declaratory ruling reaffirming that, as a legal matter, its phone-to-phone IP telephony services must continue to be exempt from access charges.[2] Level 3 has urged that rather than become mired in the difficult legal issues affecting whether access charges apply to

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[1] Voice-embedded IP communications are often referred to as "Voice-over-Internet-Protocol" or "VoIP." Level 3 uses "Voice-embedded IP" because that term more accurately describes voice as one of many applications that can be transmitted in IP format, including applications that integrate voice with data, video, or other applications.

[2] *See* Petition for Declaratory Ruling that AT&T's Phone-to-Phone IP Telephony Services are Exempt from Access Charges, WC 02-361 (Oct. 18, 2002) ("AT&T Petition").

particular kinds of voice-embedded IP communications,[3] the Commission should – at least with respect to IP-PSTN and incidental PSTN-PSTN traffic[4] – issue a decision forbearing from the enforcement of any provisions under which access charges might arguably apply. In so doing, Level 3 does not concede that access charges *are* applicable; rather, Level 3's petition simply provides a means to avoid the lengthy litigation and attendant regulatory uncertainty that would otherwise accompany resolution of these issues.[5] That, in turn, will lead to increased investment in voice-embedded IP services, greater innovation, and expanded benefits for end users.[6]

As noted above, however, Level 3 does not submit this letter to reiterate arguments for the continued non-applicability of access charges to voice-embedded IP services, but rather to address the related retroactivity issue. On November 25, 2003, Time Warner Telecom ("TWTC") submitted an *ex parte* letter arguing that whatever access regime the Commission decides to apply to *future* voice-embedded IP traffic, it should make clear that no access charges will apply retroactively to "VoIP traffic exchanged between the release of the *Report to Congress* and the effective date" of any new rule.[7] AT&T has similarly argued that "even if the Commission could . . . identify some legitimate basis for repealing the existing access charge exemption" for VoIP traffic, "there could be no possible basis to apply any such ruling retroactively."[8]

Predictably, the Bell Operating Companies ("BOCs") – which stand to benefit from a tremendous windfall if access charges are applied to VoIP retroactively – have taken the opposite position. SBC filed an *ex parte* soon after TWTC, arguing that this Commission is legally obligated to apply access charges retroactively, unless doing so would produce "manifest injustice."[9] A more recent Verizon *ex parte* made similar arguments, claiming that the Commission lacks discretion to apply access

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[3] Those issues include: 1) whether the particular kind of communication is a "telecommunications service" or an "information service"; 2) if an "information service," whether it was interconnected with the PSTN through the ESP exemption or pursuant to carrier arrangements; 3) if intrastate access charges are to apply, whether the service is intrastate in nature; 4) whether it is permissible to apply access charges pursuant to existing FCC and state rules and precedents; and 5) whether it is in the public interest to apply access charges in this context. *See* Level 3 Communications LLC's Petition for Forbearance Under 47 U.S.C. § 160(c) and Section 1.53 of the Commission's Rules from Enforcement of 47 U.S.C. § 251(g), Rule 51.701(b)(1), and Rule 69.5(b), WC 03-266 (Dec. 23 2003) ("Level 3 Petition").

[4] As explained in the Level 3 Petition, such "incidental" traffic includes a small volume of traffic that cannot feasibly be distinguished from IP-PSTN traffic. *See* Level 3 Petition at 7.

[5] *See, e.g., id.* at 4, 9, 20-31.

[6] *See id.* at 38-44.

[7] Letter from Thomas Jones to Marlene Dortch, CC Docket No. 01-92, WC Docket Nos. 02-361, 03-211 (Nov. 25, 2003), at 4 ("TWTC 11/25/03 Letter").

[8] Letter from David Lawson to Marlene Dortch, WC Docket No. 02-361 (Dec. 22, 2003), at 1-2 ("AT&T Letter").

[9] Letter from Gary Phillips to Marlene Dortch, WC Docket No. 02-361 (Dec. 19, 2003), at 2 ("SBC 12/19/03 Letter"); Letter from James C. Smith to Michael Powell, WC Docket Nos. 02-361, 03-211, and 03-266 (Jan. 14, 2004), at 4 ("SBC 01/14/04 Letter").

charges to voice-embedded IP communications on a prospective-only basis, and that AT&T seeks an unlawful "retroactive waiver" of a purportedly established rule that providers of voice-embedded IP services must pay access charges.[10]

Level 3 submits that the BOCs' retroactivity analyses are, as a legal matter, flatly wrong. SBC's letter makes clear that it relies on the flawed assumption that voice-embedded IP traffic has always been a "telecommunications service" that "is subject to section 69.5 of the Commission's rules."[11] Similarly, Verizon takes the absurd view that "*AT&T's petition presents no 'retroactivity' issue at all*" because "section 69.5(b) of the Commission's rules" has always applied to voice-embedded IP communications.[12] As set forth below, these BOC assertions are made possible only by willful blindness to the past eight years of regulatory treatment of voice-embedded IP traffic.

Level 3 begins by briefly setting forth that history. We then argue that, in light of the Commission's past treatment of voice-embedded IP communications, applying access charges retroactively would make no sense as a matter of either law or policy. Notably, however, even were the Commission to accept SBC's palpably incorrect "manifest injustice" standard for assessing the propriety of retroactive rules, this history makes clear that retroactive application of access charges *would* produce "manifest injustice."

I. Background: Past Regulatory Treatment of Voice-Embedded IP Communications

Whether the circuit-switched per-minute access charge regime applies to *past* voice-embedded IP communications does not – contrary to the claims of SBC and Verizon – depend solely on what section 69.5 might mean today if read in isolation. Rather, the retroactivity dispute must be informed by the Commission's *past* regulatory treatment of voice-embedded IP. If, as TWTC argues, the Commission has steadfastly maintained a "clear policy" of *not* applying access charges to such traffic,[13] it would be patently unfair to apply such charges retroactively. As further set forth below, TWTC's assertion is correct.

The history of the Commission's treatment of voice-embedded IP services begins with the regulatory regime already in place when such services started to emerge. That regime began to take shape in the 1970s and 1980s. As data processing services became more widespread and increasingly intermingled with communications services, the Commission was obliged to consider the appropriate regulatory treatment of the two kinds of services. That consideration culminated in 1980 in the *Second Computer Inquiry*, in which the Commission determined that "basic" transmission services would be

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10 *See* Letter from Kathleen Grillo to Marlene Dortch, WC Docket Nos. 02-361, 03-266, 03-211, and 03-45 (Jan. 22, 2004) ("Verizon 01/22/04 Letter"); *see also* Letter from Glenn Reynolds to Marlene Dortch, CC Docket No. 02-361 (Feb. 6, 2004) ("BellSouth 02/06/04 Letter"); Letter from Andrew Crain to Marlene Dortch, WC Docket No. 02-361 (Feb. 3, 2004) ("Qwest 02/03/04 Letter").

11 SBC 12/19/03 Letter at 2.

12 Verizon 01/22/04 Letter at 18 (emphasis in original).

13 TWTC 11/25/03 Letter at 3.

regulated under Title II of the Communications Act, while "enhanced" services carried over "basic" transmission services would remain largely unregulated.[14] Soon after *Computer II*, in 1983, the Commission expressly determined not to apply per-minute access charges to "enhanced" service providers ("ESPs"), initially as a temporary measure to improve the financial viability of then-nascent ESPs.[15]

Although the Telecommunications Act of 1996 did not employ the terms "basic" and "enhanced" services, it similarly distinguished "telecommunications services" from "information services," and left the latter largely unregulated.[16] Of course, the precise contours of those statutory terms remain hotly debated. Significantly, however, following adoption of the Act, the Commission indefinitely extended the exemption of ESPs (including Internet Service Providers, or "ISPs") from access charges, pending the adoption of new federal access arrangements applicable to advanced services. The Commission's 1997 *Access Charge Order* noted that "had access rates applied to ISPs over the past 14 years, the pace of the development of the Internet and other services may not have been so rapid."[17] The Commission thus intended that continued non-applicability of access charges would encourage further investment and innovation in rapidly evolving IP communications technologies.

At the time of adoption of the 1996 Act, voice-embedded IP communications were in their infancy; the first commercially available VoIP product was VocalTec's IPhone, introduced in 1995.[18] IPhone was a software product that allowed users to speak to other users of the same software via the Internet. Such early "IP telephony appeared to have few of the characteristics of traditional telephony,"[19] but rather was one of many applications used by people accessing the Internet via dial-up connections. As such, most observers agreed that these new services fell within the ESP exemption from access charges, and that there was "neither [a] need nor a justification to regulate IP telephony according to traditional telecommunications rules."[20]

Not all agreed, however. In March 1996, an industry group called "America's Carriers Telecommunication Association" ("ACTA"), representing a large number of small and medium-sized

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14 *See Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry)*, Final Order, 77 FCC 2d 384, 387 ¶ 9 (1980) ("*Computer II*").

15 *See MTS and WATS Market Structure*, Third Report and Order, 93 FCC 2d 241 (1983), affirmed *sub nom NARUC v. FCC*, 737 F.2d 1095 (D.C. Cir. 1984).

16 *See* 47 U.S.C. §§ 153(46), 153(20).

17 *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Transport Rate Structure and Pricing End User Common Line Charges*, First Report and Order, 12 FCC Rcd 15982, 16133 ¶ 344 (1997) ("*Access Charge Reform Order*").

18 *See* Ted Stevens, *Policy Essay: The Internet and the Telecommunications Act of 1996*, 35 Harv. J. on Legis. 5, 22 (1998).

19 Robert S. Metzger & Benjamin P. Broderick, "Communications Convergence," The Computer & Internet Lawyer (Oct. 2001).

20 *Id.*

interexchange carriers (but not AT&T, MCI, or Sprint) filed a petition with the FCC seeking a declaratory ruling that companies like VocalTec were providing "telecommunications services."[21] ACTA urged the Commission to order such companies to immediately stop providing services pending their compliance with Title II, and to institute a rulemaking to govern voice-embedded Internet communications.

The overwhelming majority of the comments and reply comments received by the Commission urged dismissal of ACTA's petition.[22] Some parties, however, while agreeing that ACTA's petition should be dismissed, took the opportunity to argue that continuing to exempt ESPs from access charges was inequitable, particularly with respect to voice-embedded IP communications. USTA, for example, argued:

> Voice communication over the Internet is now technically feasible and increasing. ACTA correctly points out that currently available software enables Internet access providers and other ESPs to readily offer both long distance telecommunications service (end to end voice communications) and information service. *The Internet access providers are currently using the public switched telephone network to offer their long distance service without paying access charges.* Thus, ESPs are not contributing to the recovery of the costs for the interstate use of the public switched access network as other carriers are required to do because of their exemption from access charges.[23]

USTA urged that "a rulemaking proceeding to consider access charge reform is imperative," but implied that such a proceeding should result in reform of the access charge regime for all carriers, "not . . . more regulation."[24] SBC's subsidiary Southwestern Bell Telephone Company ("SWBT") took a more aggressive tack, arguing that the Commission should either 1) immediately eliminate the ESP exemption and order ESPs providing interstate voice-embedded IP services to pay the same access charges applicable to IXCs; or 2) order the ESPs to cease providing such services without paying access charges or else incur forfeiture penalties.[25]

The FCC declined to rule on the ACTA petition, thus effectively denying it. Moreover, as noted above, in 1997 the Commission reaffirmed the ESP access charge exemption.[26] By the time Senator Stevens published an article calling for regulatory reform in the Harvard Journal on Legislation in early

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21 *See* America's Carriers Telecommunications Association Petition for Declaratory Ruling, Special Relief, and Institution of Rulemaking Regarding the Provision of Interstate and International Interexchange Telecommunications Service Via the Internet by Non-Tariffed, Uncertified Entities, RM-8775 (Mar. 4 1996).

22 *See* FARNET's Washington Update, "ACTA Petition Met With Overwhelming Opposition, FCC Likely to Dismiss" (June 21, 1996) (available at http://www.educause.edu/pub/wu/1996/0621.html).

23 USTA Comments, RM-8775 (May 8, 1996), at 2-3 (emphasis added).

24 *Id.* at 3.

25 *See* Comments of Southwestern Bell Telephone Company, RM-8775 (May 8, 1996), at 8.

26 *See Access Charge Reform Order*, 12 FCC Rcd at 16133 (¶ 344).

1998, it was common knowledge that under the "FCC's current treatment of voice communications – telephony – over the Internet," a "growing amount of voice traffic" was "not subject to Title II regulation."[27] Senator Stevens pointed out that Internet telephony was "gaining market share," and that recent innovations allowed some "information service providers" to offer customers "telephone to telephone" services.[28] He argued that the "FCC's present policies" toward Internet telephony were inconsistent with the "1996 Act's goal of competitive neutrality,"[29] and that the Commission should therefore construe the term "telecommunications carrier" to include "ISPs who offer to transmit their customers' messages," so as to resolve "the regulatory inequality between ISPs and interexchange carriers."[30] Senator Stevens' article thus reflects, in clear and authoritative terms, that the *status quo* in early 1998 was one in which "Internet telephony" – *including* new "telephone to telephone" services – was *not* subject to access charges under the "FCC's [then-]present policies."[31]

In April 1998, the FCC issued a *Report to Congress* (frequently called the "*Stevens Report*"), which addressed the Commission's implementation of the 1996 Act's universal service provisions. In addition, however, in a section entitled "IP Telephony," the *Report* considered Senator Stevens' argument – now echoed, of course, by SBC and Verizon – that voice-embedded IP communications should be treated as "telecommunications services" under the 1996 Act. The Commission began by distinguishing two basic categories of IP telephony: 1) "computer-to-computer" communications, which required users to install software on their computer and to call other users running compatible software; and 2) phone-to-phone services, which permitted calls between PSTN users via "gateways" converting circuit-switched communications to and from IP packets.[32] With respect to "computer-to-computer" communications, the Commission swiftly concluded that "the Internet service provider does not appear to be 'provid[ing]' telecommunications to its subscribers" within the meaning of the Act.[33] As to "phone-to-phone" IP telephony,[34] the Commission found that the "record currently before [it] suggests" a lack of "information services" characteristics.[35]

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27 Stevens, 35 Harv. J. on Legis. at 21.

28 *Id.* at 22.

29 *Id.* at 21-23.

30 *Id.* at 29-30.

31 In light of Senator Stevens' comments – the comments, it must be remembered, of a *proponent* of applying access charges to VoIP – Verizon's bald claim that "[e]xisting [l]aw [h]as [a]lways [r]equired AT&T [t]o [p]ay [a]ccess [c]harges on [i]ts [p]hone-to-[p]hone, [s]o-[c]alled 'IP [t]elephony' service," Verizon 01/22/04 Letter, Attachment at 1, is pure revisionist history.

32 *See* Federal-State Board on Universal Service, *Report to Congress*, 13 FCC Rcd 11501, 11541 ¶ 84 and nn. 173-77 (1988) ("*Report to Congress*").

33 *Id.* at 11543 (¶ 87).

34 The *Report* defines "phone-to-phone" telephony as services in which the provider: 1) holds itself out as providing voice telephony or facsimile transmission service; 2) does not require customers to use CPE different from that used on the PSTN; 3) allows the customer to call NAMP numbers; and 4) transmits customer information without net change in form or content. *Id.* at 11543-44 (¶ 88).

35 *Id.* at 11544 (¶ 89).

Significantly, however, the Commission nonetheless found that it was not "appropriate to make any definitive pronouncements" regarding the proper categorization of "phone-to-phone" telephony "in the absence of a more complete record focused on the individual service offerings."[36] It "defer[red] a more definitive resolution of these issues pending the development of a more fully-developed record."[37] The Commission further noted, with respect to access charges, that to the extent that it were ultimately to "conclude that certain forms of phone-to-phone IP telephony are 'telecommunications services,'" it might also "find it reasonable" that providers of such services "pay similar access charges" to those paid by IXCs.[38] "On the other hand," the Commission wrote, "we likely will face difficult and contested issues relating to the assessment of access charges on these providers."[39] The Commission concluded that it would "examine these issues more closely based on the more complete records developed in future proceedings."[40]

The *Report to Congress* thus effected no change in the *status quo* – non-applicability of access charges to voice-embedded IP communications.[41] As set forth above, access charges had never been applied prior to the *Report*'s issuance and, as TWTC explains, it was the "clear message" of the *Report* that "the Commission would not apply [] access charges to [such] traffic *until* such future time as it reached a binding decision on that issue."[42] That message was further confirmed, as AT&T pointed out in its petition, by the fact that the FCC refused to consider a post-*Report* petition filed by U S West arguing that "phone-to-phone IP telephony services" are "telecommunications services," and should be regulated by the FCC as such.[43] Indeed – in contrast to the ACTA petition in 1996 – the Commission declined even to seek comment on U S West's petition.

The Commission's subsequent statements in its *Intercarrier Compensation Regime NPRM* further confirm its consistent position regarding the non-application of access charges to VoIP.[44] There, the Commission noted that "IP telephony [is] *generally exempt* from access charges under the enhanced service provider (ESP) exemption,"[45] and suggested that the fact that "an IXC must pay access charges"

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36 *Id.* at 11544 (¶ 90).

37 *Id.*

38 *Id.* at 11544-45 (¶ 91).

39 *Id.*

40 *Id.*

41 Verizon's claim that "the *Report to Congress* could not legally have changed the Commission's rules," Verizon 01/22/04 Letter, Attachment at 10, is thus beside the point. The fact is that the *Report did not change the Commission's rules* – it merely re-confirmed the agency's existing policy.

42 TWTC 11/25/03 Letter at 4.

43 *See* AT&T Petition at 16-17.

44 *See Developing a Unified Intercarrier Compensation Regime*, Notice of Proposed Rulemaking, 16 FCC Rcd 9610 (2001).

45 *Id.* at 9613 (¶ 6) (emphasis added).

while companies "provid[ing] IP telephony do[] not" may give IP telephony providers a cost advantage.[46] The Commission also expressed concern that "Internet Protocol (IP) telephony threatens to erode access revenues for LECs because it is exempt from the access charges that traditional long-distance carriers must pay."[47] It is, of course, difficult to imagine how the Commission could more clearly have confirmed its policy that "Internet Protocol (IP) telephony . . . is exempt from [] access charges" than by explicitly so stating.

Moreover, contrary to the BOCs' present posturing, the FCC's long-standing policy that voice-embedded IP communications have never been subject to access charges was (and remains) well known and widely publicized. For years, that policy has been reported by the trade press, by academic commentators, and by the mass media. In May 2000, for example, a *Legal Times* article stated in no uncertain terms that "[i]n the United States, VoIP is treated as an unregulated information service," so "VoIP providers, unlike traditional long distance carriers, do not have to pay 'access charges.'"[48] In October 2001, an article in *The Computer & Internet Lawyer* reported with equal confidence that even "phone-to-phone Internet telephony" – which may "begin and end over an ordinary telephone handset and sound no different than a PTSN call" – nonetheless "remain[s] exempt from common carrier regulations," specifically including "access fees."[49] The 2003 Catholic University CommLaw Conspectus flatly states that "the current regulatory regime exempts IP telephony providers from the obligation to pay hefty access charges."[50] And mass media newspapers and magazines continue almost daily to report that unquestioned fact.[51] These examples could be multiplied almost infinitely, but the basic point is clear: from the inception of VoIP services to this day, the FCC policy that access charges do not apply to voice-embedded IP communications – whether IP-PSTN or PSTN-PSTN – has been widely remarked and reported. As set forth below, that history bears directly on the present debate concerning potential retroactive application of access charges, should they be found to apply to some voice-embedded IP communications.

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46 *Id.* at 9616 (¶ 12).

47 *Id.* at 9657 (¶ 133).

48 Mike Senkowski and Jeff Linder, "Is it a Zebra or a Striped Horse? Internet Telephony Challenges Traditional Regulatory Distinctions," *Legal Times* (May 8, 2000). Notably, Messrs. Senkowski and Linder were (and are) prominent ILEC lawyers, representing GTE and later Verizon.

49 Robert S. Metzger & Benjamin P. Broderick, *Communications Convergence*, The Computer & Internet Lawyer (Oct. 2001).

50 Cherie R. Kiser and Angela F. Collins, "Regulation on the Horizon: Are Regulators Poised to Address the Status of IP Telephony?," 1 CommLaw Conspectus 19 (2003).

51 *See, e.g.,* Peter Burrows, Roger O. Crockett, Steve Rosenbush, and Charles Haddad, "Net Phones Start Ringing Up Customers," *BusinessWeek* (Dec. 29, 2003) ("VoIP . . . will allow competitors like Time-Warner and AT&T to reach consumers without paying hefty access charges."); Kristi E. Schwartz, "AT&T Joins Voice Over Internet Race," *Palm Beach Post* (Dec. 12, 2003) (VoIP "calls are free from access charges"); Reinhardt Krause, "Internet Telephony Puts Bells on Hook," *Investor's Business Daily* (Nov. 24, 2003) ("Because VoIP calls use the Internet or private IP networks, service providers like Vonage avoid access charges.").

II. Discussion: Access Charges Should not Apply Retroactively

SBC argues that "it would be an abuse of discretion by the Commission" to apply access charges – assuming that they are ultimately determined to apply at all – "on a prospective-only basis."[52] But that is simply incorrect; the cases upon which SBC relies are wholly inapposite.[53] *Exxon v. FERC* involved a FERC order on remand revising its valuation methodology for crude oil in response to an earlier decision of the D.C. Circuit expressly holding FERC's methods for valuing two kinds of crude oil unlawful. *OXY USA, Inc. v. FERC*, 64 F.3d 679 (D.C. Cir. 1995). On remand, the Commission approved a settlement (proposed by various parties, but opposed by Exxon) that "corrected the legal errors identified in *OXY*," but "opted to apply the new rates prospectively only, leaving the parties without remedy for the years of unlawful valuations, and granting the settling parties a windfall."[54] Exxon argued that when a case is remanded because "the Commission commits legal error, the proper remedy is one that puts the parties in the position they would have been in had the error not been made"[55]; "it is proper to correct such legal errors retroactive to the time they occurred."[56] The court agreed, finding a strong equitable presumption in favor of retroactivity to make the parties whole *when a court has found that the Commission committed legal error.*[57]

Exxon is plainly inapplicable here. The FCC's long-standing policy exempting voice-embedded IP communications from access charges has never even been subject to judicial challenge, let alone adjudicated and held to be unlawful. Accordingly, unlike in *Exxon*, a prospective-only rule here would fall squarely within the FCC's undoubted general "discretion in determining when and if a [policy] should apply retroactively."[58] Unlike in *Exxon*, here there has been no finding of unlawful action on the part of the Commission to limit its discretion.

Verizon v. FCC is equally unhelpful to SBC. In an earlier case, *C.F. Communications Corp v. FCC*, 128 F.3d 735 (D.C. Cir. 1997), the D.C. Circuit had held that an FCC decision allowing LECs to impose End User Common Line ("EUCL") fees on certain payphone providers was unlawful. On remand, the FCC indicated its intent to hold the LECs liable for unlawfully imposed EUCL charges,

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52 SBC 12/19/03 Letter at 2; *see also* SBC 01/14/04 Letter at 9-11 (arguing that the Commission is legally required to impose access charges retroactively on "IP-in-the-Middle Long Distance Service").

53 *See Exxon v. FERC*, 182 F.3d 30 (D.C. Cir. 1999); *Verizon v. FCC*, 269 F.3d 1098 (D.C. Cir. 2001) (relying on *Exxon*); *see also* Qwest 02/03/04 Letter, Memorandum at 3 ("[T]he cases cited by SBC do not deal with the [present] situation . . .").

54 *Exxon*, 182 F.3d at 47.

55 *Id.* (quoting *Public Utils. Comm'n of California v. FERC*, 988 F.2d 154, 168 (D.C. Cir. 1993) ("*CPUC*")).

56 *Exxon*, 182 F.3d at 48 (citing *Tennessee Valley Municipal Gas Association v. FPC*, 470 F.2d 446 (D.C. Cir. 1972); *Public Service Co. of Colorado v. FERC*, 91 F.3d 1478 (D.C. Cir. 1996)).

57 *Exxon*, 182 F.3d at 49.

58 *Id.*

although it postponed the question of damages to a later proceeding.[59] The D.C. Circuit held that the agency's finding of retroactive liability "was not an abuse of discretion."[60] The court emphasized that the LECs' ability to impose EUCL fees had been "under unceasing challenge before progressively higher legal authorities" from the time it was announced until the time it was adjudicated to be unlawful.[61] An argument for "nonretroactivity . . . cannot be premised on a *single*, recent agency decision . . . that is still in the throes of litigation when it is overruled."[62] The court also pointed out that because no damages had yet been assessed, the LECs could "present[] their equitable concerns to the agency during the next phase of proceedings."[63]

Once again, in the present case – unlike in *Verizon* (and *Exxon*) – there has been no adjudication of legal error by the Commission to constrain its discretion in determining whether to adopt a prospective or retroactive rule. And even SBC does not suggest that the FCC's policy of exempting voice-embedded IP communications from access charges has been "under unceasing challenge before progressively higher legal authorities" over the past six or eight years. Nor does anyone maintain that a prospective-only rule here would be based on a "*single*, recent agency decision." Rather, retroactive application of access charges would be inappropriate because of the Commission's consistent policy dating back to the earliest days of IP telephony – set forth in Part I, *supra* – exempting all voice-embedded IP communications from access charges.

Putting SBC's mistaken reading of *Verizon* aside, the case does help to set forth the *proper* framework for analyzing retroactivity here. The *Verizon* court expressly stated that "when there is a 'substitution of new law for old law that was reasonably clear,' the new rule may justifiably be given prospective[]-only effect in order to 'protect the settled expectations of those who had relied on the preexisting rule.'"[64] Contrary to SBC's arguments,[65] a Commission decision to apply access charges to voice-embedded IP communications *would* be a "new rule." The *current* rule – which, as discussed above, has applied from the very earliest days of IP telephony – is more than just "reasonably clear." The Commission's consistent, unwavering, and oft-remarked policy – since even before the 1996 Act – has been that access charges do not apply to IP telephony. SBC and Verizon are able to argue to the contrary only by ignoring that history almost completely.

To the extent that the BOCs consider the historical backdrop of the current issue at all, they focus on the *Report to Congress*, arguing that the *Report* did not "create a new exemption" to the access charge regime.[66] On that point, the BOCs are literally correct, although their conclusions are not. As set

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59 *See Verizon*, 269 F.3d at 1100.

60 *Id.* at 1110.

61 *Id.*

62 *Id.* (quoting *Clark-Cowlitz Joint Operating Agency v. FERC*, 826 F.2d 1074, 1083 n.7 (D.C. Cir. 1987)).

63 *Verizon*, 269 F.3d at 1101.

64 *Id.* at 1109 (quoting *Williams Natural Gas Co. v. FERC*, 3 F.3d 1544, 1554 (D.C. Cir. 1993)).

65 *See* SBC 12/19/03 Letter at 2; SBC 01/14/04 Letter, Attachment at 10-11.

66 *See, e.g.,* SBC 01/14/04 Letter at 11; *see also* Verizon 01/22/04 Letter, Attachment at 9-10.

forth above, the *Report to Congress* did *not* create a new exemption to the access charge regime. Rather, by the time of the *Report*, it was well-known that under the "FCC's current treatment of [IP] voice communications" such services – including "telephone to telephone" services – were not "subject to Title II regulation."[67] The *Report to Congress* merely *reinforced* that preexisting policy, rather than "creating" any new law.

Moreover, although Level 3 believes that the Commission has consistently declined to apply access charges to *all* kinds of voice-embedded IP communications, the point is particularly clear with respect to the kinds of IP-to-PSTN and PSTN-to-IP voice communications underlying Level 3's recent Petition for Forbearance.[68] Both SBC and Verizon acknowledge that such voice-embedded IP communications are "vastly different" from the AT&T services at issue in its petition, noting that IP-PSTN communications "originate and/or terminate in IP" and "involve a net change in protocol."[69] In addition, Level 3's IP-PSTN services plainly do – in the words of the *Report to Congress* – "offer a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available"[70] packetized information.[71] Accordingly, the *Report*'s intimation that access charges might one day apply to IP-based "telecommunications services" is irrelevant to these services[72]; both before and after the *Report*, it was clear that access charges did not and do not apply to IP-PSTN services.

Verizon's argument that, with respect to PSTN-PSTN services, the application of access charges is nonetheless black-and-white is incorrect. First, as set forth above, the *Report to Congress* plainly stopped short of actually adopting a new rule applying access charges to PSTN-PSTN voice-embedded IP traffic – the *Report* merely indicated that the Commission "may" ultimately decide that access charges should apply.[73] Equally important, the *Report* recognized that the category of PSTN-PSTN services sweeps in a variety of "individual service offerings"[74]; "certain forms of phone-to-phone IP telephony" may be "telecommunications services," and other forms may not.[75] For example, as Level 3 pointed out in its petition, even the provision of IP-PSTN services may well necessitate a certain amount of "incidental" PSTN-PSTN traffic that cannot feasibly be distinguished from IP-PSTN traffic.[76] Verizon's categorical view that plain language of section 69.5(b) – which was not, of course, designed

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67 Stevens, 35 Harv. J. on Legis. at 21-22.

68 *See* n.3, *supra*.

69 SBC 01/14/04 Letter at 2; *see* Verizon 01/22/04 Letter, Attachment at 2-3 (distinguishing phone-to-phone IP telephony from what Verizon calls "true IP telephony" – *i.e.*, IP-PSTN voice-embedded communications).

70 *Report to Congress*, 13 FCC Rcd at 11544 (¶ 89).

71 *See* Level 3 Petition at 11-14.

72 *See Report to Congress*, 13 FCC Rcd at 11544-45 (¶ 91).

73 *See id.*

74 *Id.* at 11544 (¶ 90).

75 *Id.* at 11544-45 (¶ 91).

76 *See* Level 3 Petition at 7. For example, traffic that would ordinarily be terminated on a customer's IP-PBX may be "forwarded" to a particular end-user's cell phone. *Id.*

or intended to address the application of access charges to voice-embedded IP communications – somehow settles the issue is inconsistent with the reality recognized by the Commission in the *Report to Congress*: the Commission will need to examine specific services more "closely based on the more complete records developed in future proceedings."[77] In the meantime, pretending that the rules have always been clear so as to justify retroactive application of access charges is simply ridiculous.

In short, contrary to the assertions of SBC and Verizon, the proper test for whether access charges should be imposed retroactively on voice-embedded IP communications is the standard applicable to "new rules."[78] As set forth in the *Verizon* case, that standard boils down to balancing the "ill effects of retroactivity . . . 'against the mischief of producing a result which is contrary to a statutory design or to legal and equitable principles.'"[79] The *Verizon* court acknowledged that the D.C. Circuit "has not been entirely consistent" in explaining how to conduct such balancing:

> In *Clark-Cowlitz* [*Joint Operating Agency v. FERC*, 826 F.2d 1074 (D.C. Cir. 1987)], the *en banc* court adopted a non-exhaustive five-factor balancing test, *see* 826 F.3d at 1081-86 (citing *Retail, Wholesale & Dep't Store Union v. NLRB*, 466 F.2d 380, 390 (D.C. Cir. 1972)). In a subsequent case, however, we substituted a similar three-factor test. *See Dist. Lodge 64 v. NLRB*, 949 F.2d 441, 447-49 (D.C. Cir. 1991) (citing *Chevron Oil Co. v. Huson*, 404 U.S. 97, 106-07 (1971)). And in other cases, the court has jettisoned multi-prong balancing approaches altogether. *See Cassell v. FCC*, 154 F.3d 478, 486 (D.C. Cir. 1998) (declining to "plow laboriously" through the *Clark-Cowlitz* factors, which "boil down to a question of concerns grounded in notions of equity and fairness").[80]

As in *Cassell*, there is no need in the present case to "plow laboriously" through multi-prong tests to determine that a new rule imposing access charges should not be applied retroactively[81] – under *Chenery*, the core question is whether some statutory imperative requires retroactive application notwithstanding the "ill effects of retroactivity."

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77 *Report to Congress,* 13 FCC Rcd at 11544-45 (¶ 91).

78 Qwest's recent *ex parte* makes the novel argument that the Commission need not choose between tests for retroactivity at all. *See* Qwest 02/03/04 Letter, Memorandum at 2-9. According to Qwest, AT&T violated the law by declining to pay access charges for its VoIP traffic, and thereby "incurred a legal indebtedness to Qwest." *Id.* at 2. Qwest devotes its energies to arguing that the Commission lacks authority to "cut off" a purported right to "collect" that debt. That argument, however, skips a critical step – it is relevant only if the Commission's policy has been (as SBC and Verizon argue) to apply access charges to voice-embedded IP communications, thus giving rise to the "debt" in the first place. As set forth in Part I, *supra*, however, that argument is flatly contrary to historical fact: the fact is that the Commission has *never* applied access charges to voice-embedded IP communications, and that policy has been widely and consistently remarked and reported by authoritative sources.

79 *Verizon*, 269 F.3d at 1109 (quoting *SEC v. Chenery Corp.*, 332 U.S. 194 (1947)).

80 *Id.* at 109-10.

81 TWTC does "plow through" the five-factor test, however, and correctly shows that the factors weigh heavily against retroactivity. *See* TWTC 11/25/03 Letter at 4-7.

The answer is clearly "no." On the one hand, no BOC advances *any* statutory requirement in urging retroactive application of access charges. Rather, they invoke only section 69.5(b) of the Commission's rules[82] – which, as set forth above, has *never* been applied to impose access charges on voice-embedded IP communications. On the other hand, the "ill effects" that would flow from wanton post-hoc regulation are patent. Indeed, the immediate, practical impact would be enormous. Expensive and protracted rounds of auditing and estimating, and of arguing and litigating, would be necessary to determine what voice-embedded IP communications exchanged since the inception of the technology should be subject to access charges. And ultimately, a precise determination would be impossible – it would simply boil down to well-heeled incumbent LECs doing their utmost to maximize the costs of their less financially secure rivals and potential rivals.

The incentive effects of retroactive regulation would be even more troubling. As TWTC set forth in its letter, "an entire industry segment has developed around the expectation that access charges do not currently apply to any VoIP traffic."[83] Given the niche nature of voice-embedded communications services to date, that segment is, of course, substantially comprised of relatively small companies seeking to bring new, innovative service offerings to consumers. Imposing access charges on such companies notwithstanding consistent FCC policy to the contrary would not only unfairly punish and impoverish them for their innovation,[84] but would obviously chill future investment by setting a troubling precedent regarding this Commission's willingness to engage in unpredictable and unfair retroactive regulation.

Ultimately, consumers would be the real losers. As Chairman Powell has recently observed, "Internet Voice will unleash a torrent of innovative products and services, from many more sources than we are accustomed to, if we let it."[85] The BOCs understandably fear that "torrent," and seek to stem it. But this Commission should not lend its aid; rather, as it recognized in exempting ESPs from access charges in 1983 and in continuing that exemption in 1997, the Commission should take steps to *encourage* (not discourage) further investment in new technologies like the rapidly evolving IP communications applications that are now starting to be deployed.

It also bears emphasis that even under the legally improper "manifest injustice" test for retroactivity proposed by SBC,[86] this Commission should still reject retroactive application of access

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82 *See, e.g.,* SBC 12/19/03 Letter at 2; SBC 01/14/04 Letter at 1-3; Verizon 1/22/04 Letter, Attachment at 4.

83 TWTC 11/25/03 Letter at 5.

84 TWTC correctly points out that financial hardship is a factor properly weighed against the retroactive application of a new rule. *See, id.* at 6 & n.15.

85 Remarks of Chairman Michael K. Powell, "The Age of Personal Communications: 'Power to the People,'" National Press Club (Jan. 14, 2004) (available at *http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-242885A1.pdf.*)

86 *See, e.g.,* SBC 12/19/03 Letter at 2. Again, however, this standard is inappropriate because applying access charges to voice-embedded IP communications would obviously be a "new rule," departing from many years of settled FCC practice. In addition, as SBC acknowledges, *id.*, that standard arose in contexts where it was

charges to voice-embedded IP communications. SBC is able to argue to the contrary only by ignoring the core historical fact set forth in detail above: the Commission's consistent policy, from the earliest days of voice-embedded IP communications, has been to *not* apply access charges to such communications:

> This is a situation, therefore, in which the question of whether to apply interstate carrier access charges has been addressed in the past by the FCC, where the . . . policy of applying access charges in the future would represent a 180 degree change from prior policy, and where numerous firms have planned their businesses up until now in reliance on the past FCC policy.[87]

In these circumstances, Level 3 believes that this Commission *should* find (and that a reviewing court *would* find) that it would be "manifestly unjust" to apply access charges retroactively – even if the Commission were to adopt that improper standard.

Sincerely,

/s/

John T. Nakahata
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necessary to "make the parties whole." Clearly, in this context, there is no need to make SBC "whole" because, as AT&T points out, SBC *has already been compensated* at "one of the several different rate regimes that the Commission has endorsed as compensatory for . . . use of the network." AT&T 12/22/03 Letter at 5.

87 *Id.*